General Dynamics Annual Report 1967

AR25

Cover: One wing of an F-111A is positioned for mating with fuselage yoke. Holes in each (emphasized by white areas in center) must be perfectly aligned. Cylinder at extreme left of picture is an 8.5-inch high-strength steel pin which will fit exactly into holes, and on which wing will actually pivot.

General Dynamics Report for the year ended December 31,1967

Results in Brief	1967	1966
Net Sales	$2,253,336,241	$1,796,990,612
Profit Before Income Taxes and Gain on Disposition of Securities	84,489,136	89,670,426
Income Taxes	33,200,000	35,716,000
Income Before Gain on Disposition of Securities	51,289,136	53,954,426
Gain on Disposition of Securities Less Applicable Taxes	5,736,576	4,452,147
Net Income	57,025,712	58,406,573
Per Common Share: Income Before Gain on Disposition of Securities	4.91	5.16
Per Common Share: Gain on Disposition of Securities Less Applicable Taxes	.55	.43
Per Common Share: Net Income	5.46	5.59
Working Capital	165,461,341	157,541,900
Property, Plant and Equipment—Net	284,905,374	237,754,430
Expenditures for Property, Plant and Equipment	96,950,500	62,099,650
Long-Term Debt	125,886,208	131,249,495
Share Owners' Equity	336,086,188	286,101,712
Equity Per Common Share	32.21	27.71
Backlog of Orders	2,372,000,000	1,651,000,000
Common Shares Outstanding	10,435,706	10,324,596

To the Share Owners:

1967 was another year of growth for General Dynamics. Sales were up 25% to a new high. Our backlog of funded orders was up 43% from 1966. Expenditures for new plant and equipment were at a record $97,000,000.

Net income for the year was down slightly.

The decline was concentrated in a few of our multiple operations. The reasons have been identified, and are being brought under control.

Consolidated sales of General Dynamics Corporation and subsidiaries for the year ending December 31, 1967 were $2,253,336,000. This compares with sales in the preceding year of $1,796,991,000. The largest gain was in military aircraft.

Deliveries to Government services and agencies represented approximately 83% of total sales in 1967.

Sales to industrial and commercial customers accounted for approximately 17% of total sales. This includes commercial communication equipment, coal, lime, building materials, machinery and compressed gases.

Aircraft and components represented 49% of total sales; marine systems 16%; military electronics and tactical missiles 12%; and space vehicles and related activities 6%.

Backlog of orders at the end of 1967 was $2,372,000,000. The year before it had been $1,651,000,000. Backlog includes only amounts actually funded and not those for orders under negotiation or unfunded on multiyear production contracts.

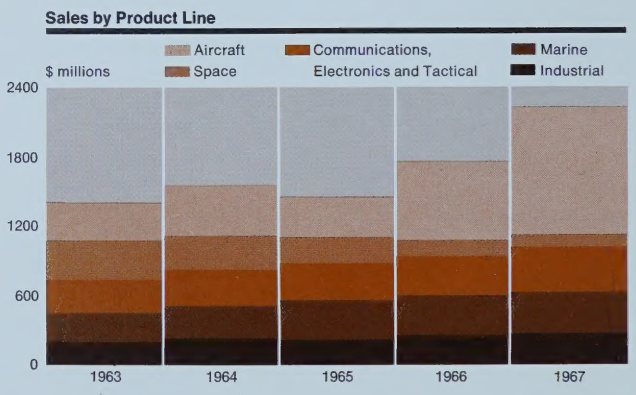
Consolidated net income for the year ending December 31, 1967 was $57,026,000, equivalent to $5.46 per common share. Of this total, $51,289,000 represented net income from operations and $5,737,000 represented nonrecurring gains from the sale of securities. Net income in 1966 was $58,407,000, equivalent to $5.59 per common share, and included $4,452,000 in nonrecurring gains.

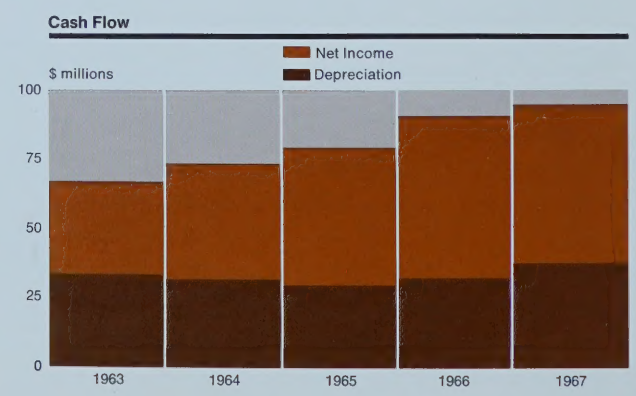
Earnings did not keep pace with the increase in sales due largely to two factors.

The first was costs in marine operations.

Most of our marine work, for both surface ships and submarines, is currently on a firm fixed-price basis, obtained on close competitive bidding, for ships which take several years to construct. Costs of these contracts are now expected to exceed earlier estimates.

Consistent with customary accounting practice, we have absorbed during the 1967 year all identifiable losses—totalling $18,700,000 after taxes—on contracts for





submarines and surface ships, some of which will not be delivered for two or three years.

An important part of the losses arose from substantial expenses incurred in the rapid buildup of facilities and manpower at our surface ship facility. This has been necessary, not alone because of the considerable amount of business we have already received, but also to prepare ourselves for important surface ship contracts in the future.

The second factor is the level of profit accruals on our F-111 contracts.

The contract for the research, development, test and evaluation phase, including 23 F-111 aircraft, was originally awarded in letter form in November 1962 and is now nearing completion. Based on experience to date and a reevaluation of costs to complete, we have revised downward the rate of profit recorded on the RDT&E contract.

Our production contract, for an initial 493 airplanes, was formalized on May 10, 1967. Deliveries have only recently commenced and will run for several years. We are recording profits on this contract at a rate which we believe realistic. Ultimate profits on such a large program cannot be accurately determined at this stage of production buildup.

The specialized nature of our organization and facilities makes General Dynamics, to a considerable degree, a committed defense contractor. Our strength is broad in the sciences and technologies essential to the development and production of modern weapon systems.

We play an important role in the national defense structure; we believe that we are considered capable and responsive to defense requirements; we believe we have the flexibility to adjust to the rapidly changing technology for which our Government and our Department of Defense must constantly be prepared.

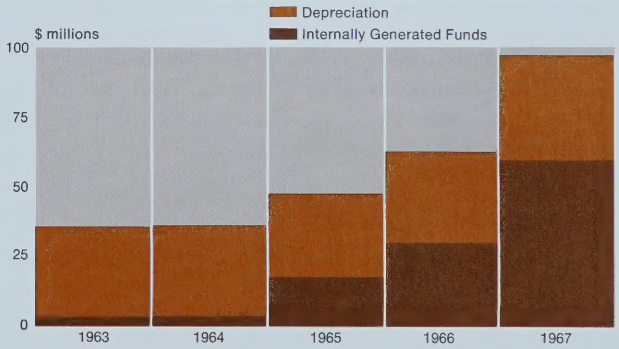
These needs will continue to have first call on our resources.

Nevertheless, we believe that a more equal balance between Government work and commercial work is desirable. We plan to seek that balance both through internal development and through acquisition of other companies that will complement our existing facilities and expertise.

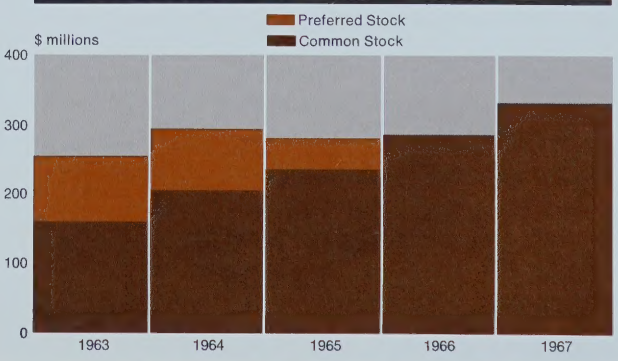
As an example of internal growth we have recently established a new division of the company to exploit our growing strength in systems capable of extremely rapid retrieval and dissemination of computer generated data.

These data systems supply immediately useful information on which to base decision-making by either management or scientists and engineers.

Capital Expenditures



Share Owners' Equity



The equipment, sold under the Stromberg-Carlson label, has been well received. Sales are increasing rapidly. New manufacturing space has been acquired and we expect important growth in this new and exciting field.

Similarly, we are expanding our coal operations. We expect to complete in 1968 a new deep shaft mine, for Freeman Coal, that will supply some 3,000,000 tons a year from our large reserves of low sulphur coal. The demand for low sulphur coal is increasing since it causes less air pollution in utility operations and because of the proximity of our supplies to a rapidly expanding metallurgical market.

During 1967, we invested approximately $97 million in new or improved facilities throughout the company.

We continued to expand and improve our nuclear submarine overhaul and refueling facilities at Electric Boat division, and completed a 610-foot graving dock capable of handling two Polaris submarines simultaneously. Land adjacent to our shipyards at both Quincy and Groton has been purchased to permit improvement of facilities. New high capacity machine tools were put in operation at both Canadair Limited and Convair division. At our Fort Worth division, a new engineering building, almost one-half-million square feet of additional manufacturing space, flight line, and flight test data processing facilities were completed. Substantial facilities for production of lime products have also been added by Marblehead Lime and for various building materials by Material Service division.

Late in the year, we sold General Atomic division, our research center for commercial nuclear power applications, to Gulf Oil Corporation. The General Dynamics concept of electrical power generation through a high temperature gas-cooled reactor (HTGR) was proven with the prototype which began producing electricity in 1967 for the Philadelphia Electric Company at Peach Bottom, Pa. Contracts for a larger commercial-sized plant in Colorado had been signed. The sale included all subsidiary programs of General Atomic division as well as power-generating reactors. Nuclear research and development already being actively pursued at other General Dynamics divisions will continue.

Considerable capital and human resources would have been required over a period of years to establish a position of leadership in the public utility power field. These resources, we believe, can be more productively employed in the fields in which the company is already established, or in new fields more directly related to our primary technologies, organization and facilities.

Research and development costs of the General Atomic division had been charged against income as they occurred from year to year. The actual sale price was greater than the book value of the division. A gain was not recorded in 1967 because certain contingencies related to the sale will not be fully resolved until later in 1968.

Early in 1968, a plan for transfer of our Liquid Carbonic Corporation subsidiary to Houston Natural Gas Corporation was approved in principle by both companies. We are required to divest ourselves of Liquid Carbonic under a 1966 consent decree.

Consummation of the transaction is subject to approval of the Justice Department and stockholders of Houston Natural Gas and to the receipt of favorable Internal Revenue Service rulings that neither the company nor its share owners would incur any tax liability on the transaction.

Two of our longtime directors, I. M. Laddon and Bernard Emmet Finucane, will retire from service as active directors at the end of their formal terms in April. Mr. Laddon had been associated with us and predecessor companies for 37 years. Mr. Finucane has been associated with General Dynamics since its merger with Stromberg-Carlson in 1955, and had been a director of that company previously. Both have been of great service to General Dynamics and have consented to continue to act as advisory directors.

We have a sound base for expansion and we see opportunities to enlarge our commercial business both in existing product lines and through carefully chosen acquisitions.

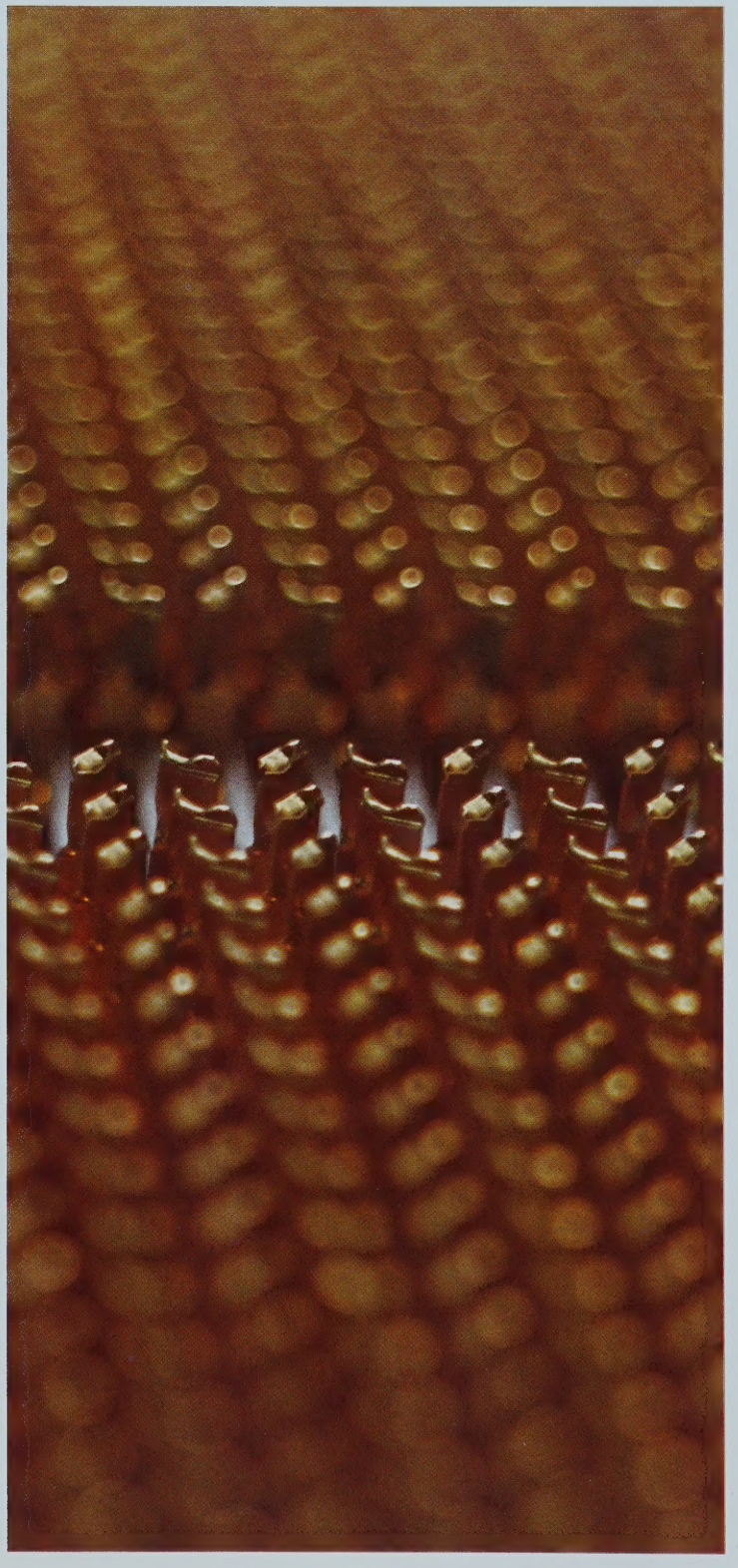
We know the coming year will bring us new challenges and new opportunities; our organization faces them with confidence.

Roger Lewis, President
January 31, 1968

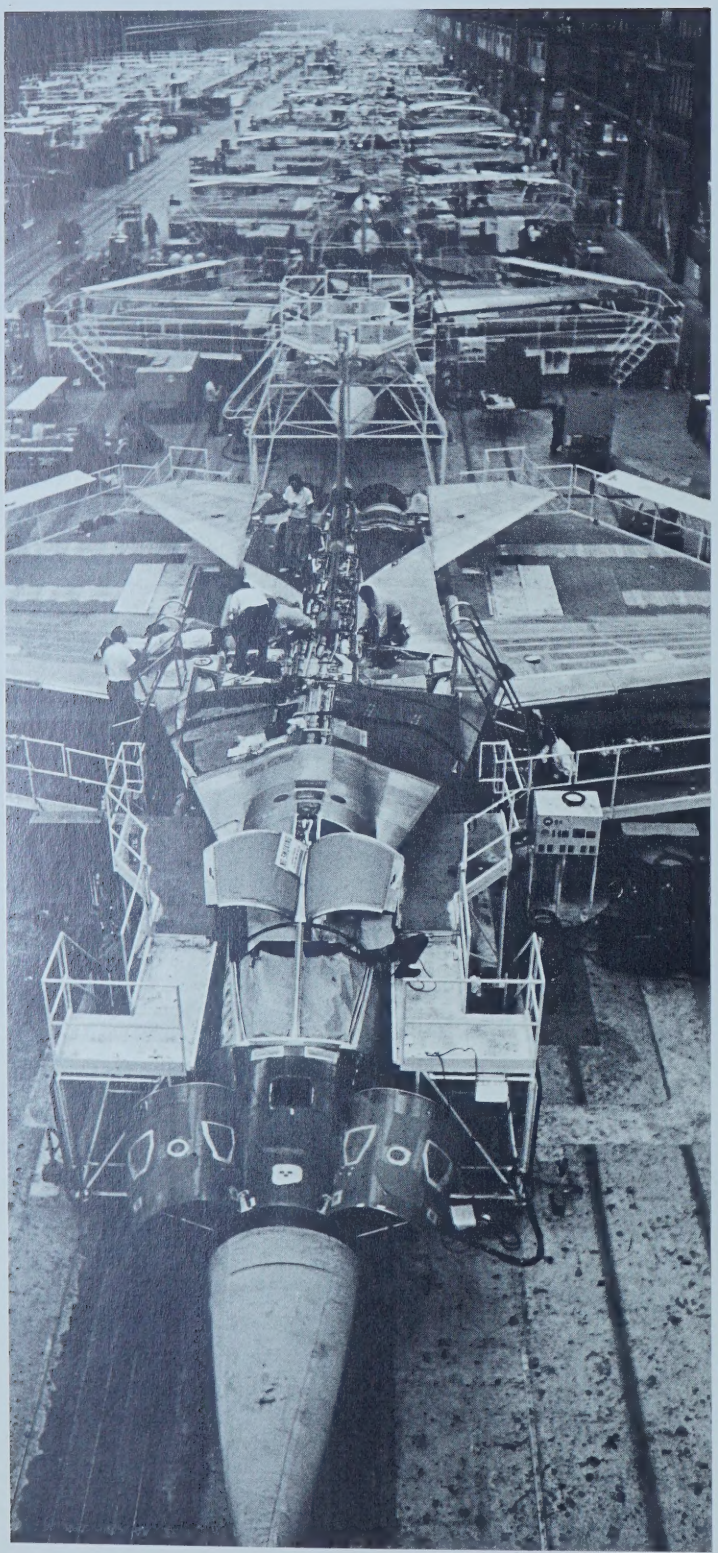
Every major system starts with the work, thought, and even the arguments of scientists, engineers, and designers.

F-111 cockpit dials and instrumentation are checked out on the assembly line for proper integration with sophisticated systems.

Hundreds of gold plated prongs
(for best electrical conductivity)
are used for test check
equipment of military avionics.



With scores of F-111s now in assembly, the production line seems to stretch into infinity at the Fort Worth plant.



Part of a giant aircraft comes out of one of the world's largest autoclaves, at the Canadair Limited plant in Montreal.

Aircraft

In May 1967, the Department of Defense signed a fixed-price incentive contract with General Dynamics for the production of an initial 493 F-111 aircraft in several configurations, at a target price of $1,821,938,561. This contract does not include the cost of equipment furnished by the Government: including engines, such weaponry as the Phoenix missile system or certain modifications and additions which have been agreed upon but not yet negotiated as to price.

Currently 55 F-111s (including the initial test versions) have been flown, another 40 are in final assembly, and many others are in various stages of construction. Production models of the F-111A are now being delivered to the Tactical Air Command of the United States Air Force.

In late December an RF-111A (a reconnaissance version) made its maiden flight. Earlier in the year a developmental FB-111A (strategic bomber version) started flight test. A test model of the F-111B (the Navy version) will undergo carrier tests in 1968.

To what degree, if at all, cancellation of the British order for 50 aircraft will affect the long-term program cannot now be anticipated. Versions for the Australian Government are already under construction.

In both test and training flights the F-111A has shown an *overall capability* substantially greater than any existing fighter aircraft, or any now known to be on the drawing boards, in its *combination* of relatively short takeoff and landing, speed variability, range, payload, navigational accuracy, precise weapon delivery and penetration to target in all weather, day or night. Pilots who have been flying the plane in the first Air Force operational unit are enthusiastic about its flying, fighting and reliability qualities.

CF-5 fighters being built at Canadair under license from Northrop Corporation are starting flight test. The Canadian Government has ordered 115 and an additional 105 are to be produced for the Royal Netherlands Air Force.

Marine

Overall, our marine business declined slightly.

Surface ship work was up; submarine work, with the completion of the 41st ship of the currently authorized Polaris fleet, declined enough to offset that gain.

During the year we delivered one Polaris-type submarine and four attack submarines and completed major retrofitting of two early Polaris-type submarines.

Currently, we have under construction or contract nine attack submarines, three research submarines, including the first nuclear-powered research submarine, and conversion of three ballistic-missile-firing submarines. One is the first to be retrofitted to accommodate the new Poseidon missile.

The initial surge to get the nuclear Polaris submarine fleet into being and operational is now largely over. Nevertheless, we anticipate continued new submarine business for attack and special types and for conversion of existing nuclear submarines to upgraded performance in line with the newest developments.

Surface ship work during the year included the christening of two Navy ammunition ships and one submarine tender and the keel-laying of a dock landing ship and a submarine tender. In addition, two tracking ships for NASA's Apollo program were deployed and additional electronic components were added on a third ship.

During the year we received contracts for an additional dock landing ship and two replenishment fleet oilers. Currently we have under construction or contract 14 large surface vessels for the United States Navy, most of them in the support-ship category.

Our surface shipyard is being systematically reorganized to take advantage of new techniques. Computer-tape-controlled machinery and automatic welding equipment have been installed. Facilities are being planned or constructed in which entire sections of ships can be built and outfitted (with piping, ventilation, wiring, machinery) indoors and the completed section moved to the building basin for installation. This technique makes shipbuilding less vulnerable to the vagaries of weather and provides additional fabrication capacity and flexibility without tying up water frontage.

Three ocean buoy data systems have been proved at sea, two for the Office of Naval Research and one for the United States Coast Guard. They have demonstrated capability for long-range transmission of automatically collected data on meteorological and oceanographic conditions and reliable operation as a navigation aid.

Research submarines were in frequent use last year on lease to various arms of the United States Government and to oil companies and other private businesses.

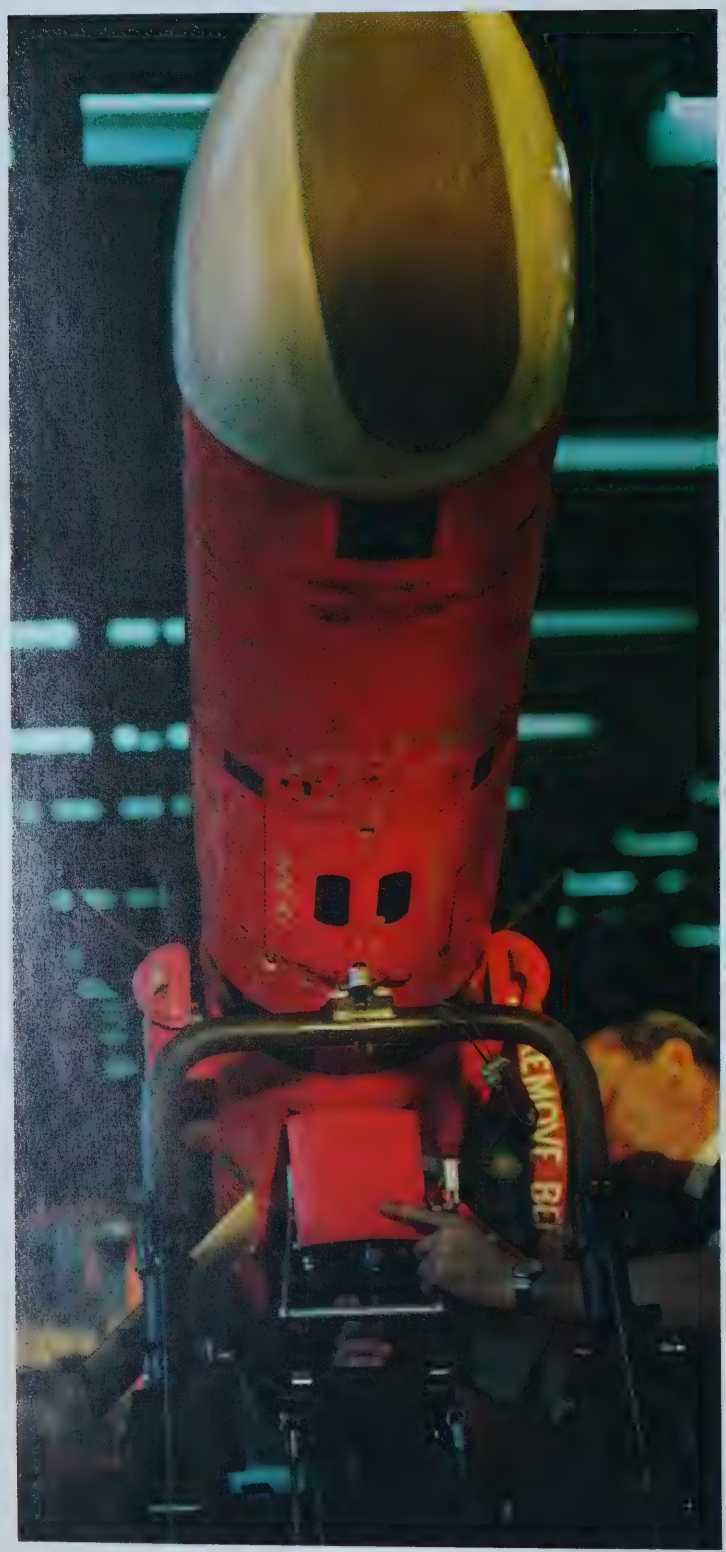
Electronics

Only one of our 14 operating units is specifically designated with the generic term "electronics," but important work in that field actually goes on at eight.

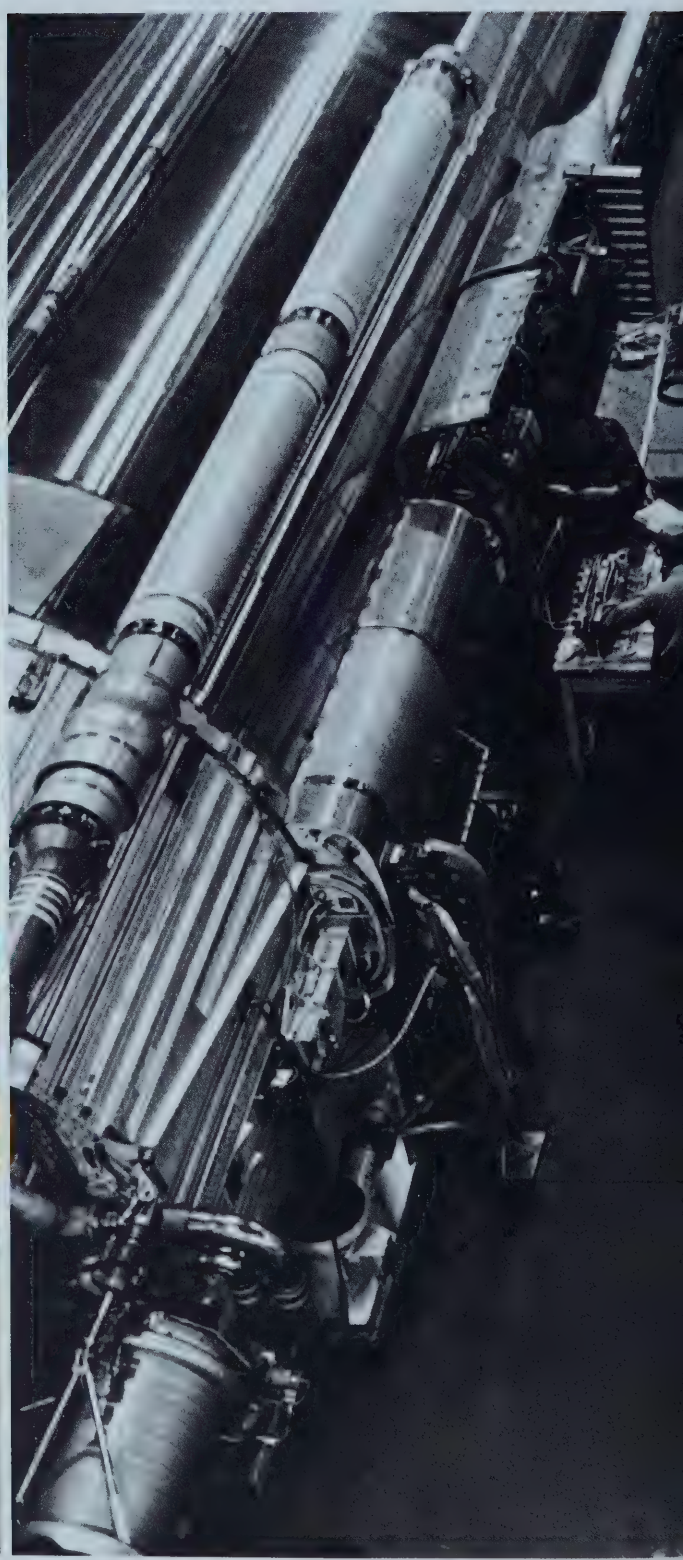
Peripheral data processing equipment use is growing rapidly. The heart of our data line is output equipment which can convert data, as fast as a computer can process it, into tabular or chart material and present it visually or on paper copy or microfilm/microfiche

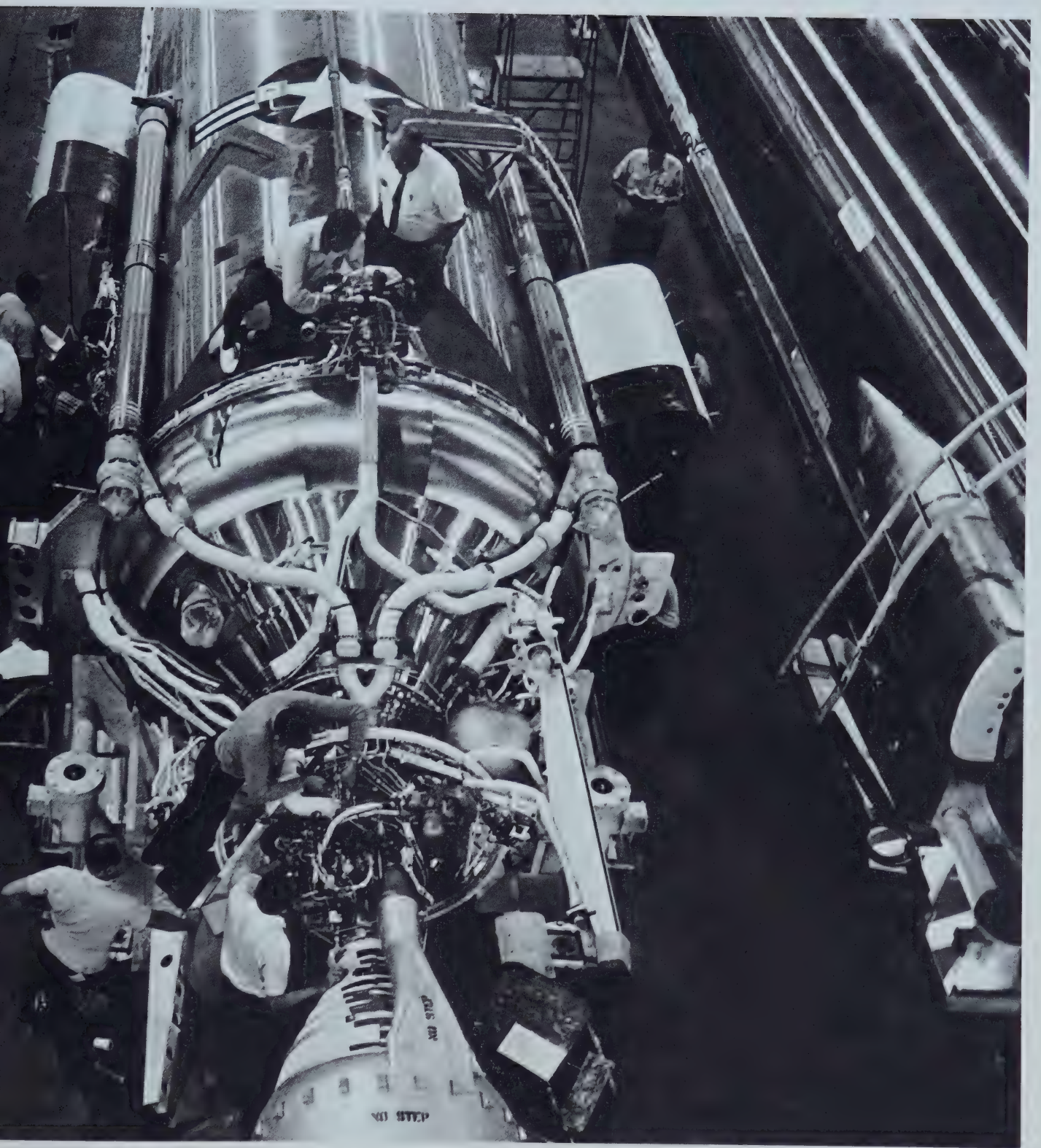
Electronic microcircuits start out as giant drawings which will be photographically reduced for perfect accuracy.

An engineer makes final adjustments to a CL-89 battlefield reconnaissance drone before it is packaged for delivery.



Fuel lines and guidance circuits of Atlases (right and left) and Centaur (center) are checked out prior to a mission.





The newest in commercially available telephone switching—a #5 crossbar office frame—has final interconnections added.

High-grade low sulphur coal is loaded on automatic conveyor system at a deep-shaft Freeman Coal Mining Corporation mine.

An extremely low vibration motor, vital for both military and industrial use, moves down the transfer line at Avenel, N.J.

A submarine model is prepared for echo-profile testing in the world's largest indoor sonar tank, at our Electronics operation.

for immediately useable information. Our commercial sales in this area have been growing rapidly.

Military electronics sales, which increased 20% in 1967, are based largely on electronic communications.

Tactical radios with thousands of channels for battlefield communications are now being delivered in quantity. Other substantial contracts include: mobile field communication centers able to handle simultaneously voice, teletype and digital transmission; radars, both airborne and ground-based; surveillance systems; terminals for the United States Army's worldwide automatic digital network (AUTODIN); and space communication and telemetry equipment.

Other production includes: microminiature circuitry; missile guidance; automatic test equipment; and antisubmarine warfare measures.

Space

Sales of space products declined, offset somewhat by an increase in research and engineering study contracts.

Continued research on satellite vehicles, life sciences, space communications and new propulsion techniques is probable. In all these fields General Dynamics has considerable experience and a solid team of scientific personnel. When new space programs become active, we will be in position to utilize our expertise rapidly.

Our products have been very active in the space program. All research spacecraft now on or orbiting the moon were launched by General Dynamics' Atlas. In a number of these missions Atlas was used in combination with our hydrogen-fueled Centaur.

Atlas was used for Project Ranger, which produced the first closeup photographs of the moon, and Project Lunar Orbiter, which produced pictures of possible landing sites for the Apollo spacecraft. In combination with Centaur (the latter the first high-energy hydrogen-fueled upper stage) both vehicles performed flawlessly in all seven launches of Surveyors to the moon.

Uprated versions of Atlas capable of launching larger payloads are currently in production. Centaur, currently the only high-energy upper stage adaptable to all larger launch vehicles in the United States inventory, is also being improved.

Telephones

During 1967, new Stromberg-Carlson telephone exchanges were installed at a rate of more than one each working day. The subsidiary has increased sales and earnings for three years in a row.

A large part of the 1967 improvement was due to the introduction of new equipment, chiefly #5 crossbar switching and T-Carrier transmission.

The T-Carrier is a solid state trunk carrier system for interconnecting central telephone offices. Pulse-code modulation carries 24 voice channels on two telephone cable pairs and minimizes noise, cross talk and voice distortion. The #5 crossbar common control switching system offers faster and more economical service for medium and large size telephone offices. This system represents the next generation after traditional step-by-step switching.

During the year Stromberg-Carlson also introduced a number of other products including: direct inquiry to a computer by telephone with a voice response answer; a compression system that allows addition of a number of teletypewriter channels on a single line without loss of voice circuitry capacity; and a complete line of the latest designs of telephone instruments. Improvements to switching systems and new switching-system controls were introduced to extend the life of XY systems already installed.

Tactical Weapons

Traditionally, General Dynamics has been a supplier of tactical missiles to the Navy for antiair warfare. Today we are developing or delivering sophisticated tactical missiles for the Navy, the Army, the Air Force and the Marines in surface-to-air, air-to-surface, surface-to-surface and air-to-air versions.

During 1967 General Dynamics won a $120,000,000 competitive contract for initial production of Standard Missile. We also obtained production contracts for an Anti-Radiation Missile (ARM).

Standard Missile is a supersonic all-electric homing missile. It has been developed to meet both surface-to-air and surface-to-surface requirements of the United States Navy. Eventually, it will replace existing Terrier and Tartar missiles and will be used on some 50 United States Navy vessels, particularly destroyers, frigates and escorts.

ARM is an air-to-surface antiradar missile equipped with a sensitive radiation-homing device and a conventional explosive warhead. It will be used by Navy and Air Force aircraft to locate and destroy hostile ground-based radar installations.

The shoulder-fired Redeye missile, developed to give combat troops protection against attack from low flying aircraft, is now being delivered in sizable quantities to the United States Army and Marine Corps. The Swedish Government has announced its intention to use Redeye missiles in its Army's antiaircraft units.

The CL-89, a battlefield photographic surveillance drone, has been ordered by the Government of Canada on behalf of three partners, Canada, Great Britain and the Federal Republic of Germany under a "production authorization," equivalent to a United States letter contract.

Resources
In spite of poor weather, strikes in customer industries, reduced steel production and severe price competition combined, overall sales and earnings of our resources operations held firm.

A series of capital improvements invested in this area should begin taking effect shortly.

Several new kilns—for lightweight aggregate, lime and brick —will go into operation in 1968, and the modernization of our fleet of Redi-Mix trucks is progressing.

Production from our new deep mine in southern Illinois, designed ultimately to produce more than 3,000,000 tons of metallurgical grade coal a year, is scheduled to start in 1968.

Divestiture
On February 2, 1968, the company and Houston Natural Gas Corporation reached agreement in principle on a plan under which Houston Natural would acquire our Liquid Carbonic Corporation by merger. The company is required by a 1966 Federal district court order to divest itself of Liquid Carbonic.

Houston Natural would issue 1,076,000 shares of new convertible preference stock and would assume $49,700,000 of existing long-term debt of General Dynamics. The new convertible preference would have an annual dividend of $2.25 a share, and would be convertible at any time into one share of Houston Natural common. The preference shares would be redeemable after five years at $52.50 a share, and would have a liquidating value of $50 a share.

The plan provides that the company, as the owner of all the outstanding stock of Liquid Carbonic, would enter into a formal merger agreement with Houston Natural and would vote its shares for the merger, subject to the conditions of the agreement. On the merger, the Liquid Carbonic shares would become Houston Natural convertible preference shares on a one-for-one basis.

Prior to the effective date of the merger, the company would make a tax-free transfer to its share owners of its Liquid Carbonic shares, and the related right to receive Houston Natural shares, either by giving its share owners the opportunity to exchange General Dynamics shares for Liquid Carbonic shares on a basis to be determined, or by a pro rata distribution, or by a combination of both. Immediately after the merger becomes effective, certificates for Houston convertible preference shares would be distributed tax-free to the holders of the Liquid Carbonic shares.

Antitrust Action
Late in 1967 the Justice Department filed an antitrust action seeking divestiture of The United Electric Coal Companies under Section 7 of the Clayton Act. The company does not believe there has been any violation and is resisting the action. Although United Electric Coal did not become a wholly owned subsidiary of General Dynamics until 1966, the essential relationship between Freeman Coal and United Electric dates back to 1960. It is General Dynamics' view that, rather than resulting in diminution of competition in the area served, the United Electric/Freeman relationship strengthened competition.

Employes
Employe rolls passed 100,000 for the first time since 1961.

More than 71% of all employes eligible, both salaried and hourly, have joined the employe savings plan. Since this relatively new plan is essentially a long-term method of accumulating savings, the large participation is indicative of the faith General Dynamics people have in the future.

The program to identify and train present and future management personnel for the company, and to improve opportunities for all individuals, is working well.

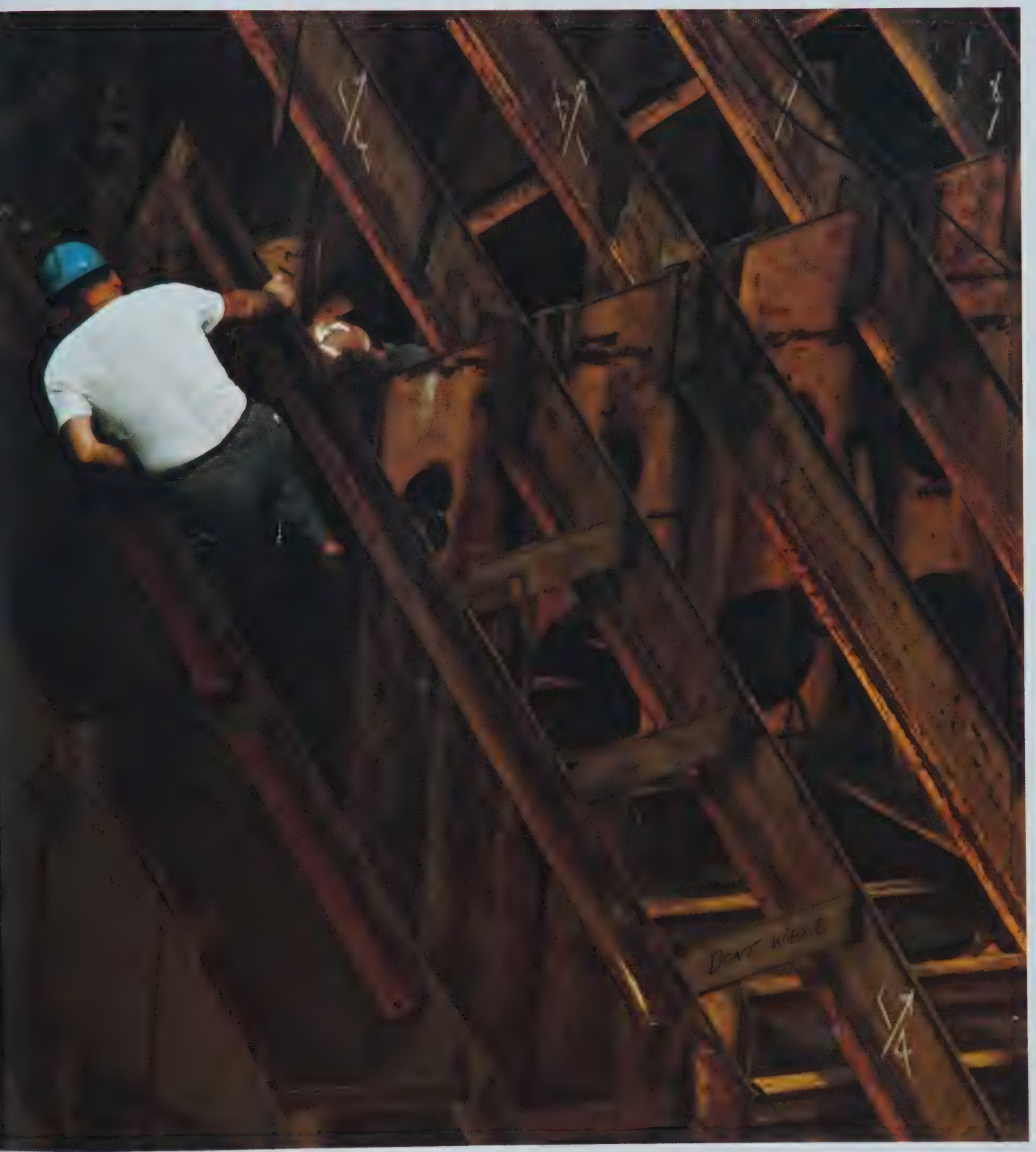
During the year approximately 22,000 persons received promotions; in line with our policy of utilizing specialized talent within the company at any point where it may be needed, approximately 1,700 interdivisional transfers or temporary duty assignments were made.

In addition, General Dynamics has been sharply aware of the need to provide training and job opportunities in areas where underemployment may be a problem.

The first graduates of a training program in the Boston area are starting work at the Quincy shipyard now.

An on-the-job training program, cosponsored with the Texas Employment Commission and the Texas Education Agency, has more than 300 of its graduates now working for General Dynamics. At Fort Defiance, Ariz., a new plant for electronic assembly ultimately will employ several hundred Navajos. In San Antonio, Tex.—one of the cities designated by the Government in its Job Development Test Program—we will train and hire hard core unemployed for light manufacturing in support of F-111 production.

A welder braces himself between giant ribs of a huge ammunition supply ship as he reaches deep to join key parts together.



A nuclear submarine is retrofitted and refueled in a huge graving dock at the Electric Boat division in Groton, Conn.

"Instant information" is copied from a microfiche reader literally within minutes after the data had been processed by a computer.

Pretty technician wires a component that will become part of a mobile tactical field radio with thousands of channels.

At day's end, shipyard workers descend a gangplank from upper decks of a giant fleet-support ship they are building.

Financial History 1958-1967

Dollars in Thousands	1967	1966	1965
Net Sales	$2,253,336	$1,796,991	$1,472,785
Profit (Loss) Before Income Taxes and Gain on Disposition of Securities	84,489	89,671	85,739
Income Taxes (Credit) (1)	33,200	35,716	36,470
Income (Loss) Before Gain on Disposition of Securities (1)	51,289	53,955	49,269
Gain on Disposition of Securities Less Applicable Taxes	5,737	4,452	—
Net Income (Loss) (1)	57,026	58,407	49,269
Per Common Share: Income (Loss) Before Gain on Disposition of Securities (2) (4)	4.91	5.16	4.48
Per Common Share: Gain on Disposition of Securities Less Applicable Taxes	.55	.43	—
Per Common Share: Net Income (Loss)	5.46	5.59	4.48
Preference Dividends (2)	—	661	8,602
Common Dividends	10,382	10,290	10,077
Working Capital	$ 165,461	$ 157,542	$ 183,613
Property, Plant and Equipment—Net	284,905	237,754	210,160
Expenditures for Property, Plant and Equipment	96,951	62,100	48,579
Long-Term Debt	125,886	131,249	110,034
Share Owners' Equity	336,086	286,102	282,827
Equity Per Common Share (3) (4)	32.21	27.71	23.35
Total Payrolls	$ 859,846	$ 763,438	$ 697,037
Employes	103,196	93,196	84,600
Share Owners of Record	54,145	63,104	66,813
Preference Shares Outstanding	—	—	787,268
Common Shares Outstanding	10,435,706	10,324,596	10,152,968

Notes:

(1) Income taxes and net income are before tax reductions of $16,917,000 in 1963 and $23,850,000 in 1962 resulting from 1961 loss carry forward. These tax reductions have been added to the income tax credit and deducted from the net loss for 1961. In addition, the 1961 net loss has been further reduced by the $33,000,000 special credit recorded in 1963. This special credit resulted from reduction in losses provided in 1961 on the commercial jet transport program by reason of cost reductions and performance achievements subsequently realized.

(2) Dividends on the convertible preference stock issued in 1959 were cumulative from and after January 1, 1964, at the annual rate of $2.90625 per share. Dividends on convertible preference stock paid in 1965 included $3,768,858 for 1965 and $4,833,512 for 1964. Net income per common share is after deducting dividends applicable to preference stock. In April, 1966, the Corporation redeemed all shares of convertible preference stock then outstanding.

(3) Share owners' equity per common share has been computed by deducting the liquidating value of outstanding convertible preference stock and accrued unpaid dividends.

(4) Amounts per common share for 1958 are not shown, as they could not be determined without making arbitrary assumptions with respect to the convertible preference stock issued in accordance with the merger with Material Service Corporation.

1964	1963	1962	1961	1960	1959	1958
$1,579,862	$1,415,074	$1,898,482	$2,062,378	$1,987,749	$1,811,871	$1,626,015
77,508	64,206	58,484	(135,067)	(61,771)	54,156	90,739
34,897	31,416	29,475	(65,630)	(34,715)	23,100	42,344
42,611	32,790	29,009	(69,437)	(27,056)	31,056	48,395
—	—	—	—	—	—	—
42,611	32,790	29,009	(69,437)	(27,056)	31,056	48,395
3.77	3.28	2.90	(6.95)	(2.71)	3.12	—
—	—	—	—	—	—	—
3.77	3.28	2.90	(6.95)	(2.71)	3.12	—
—	—	—	—	—	—	—
—	—	—	2,494	14,919	19,881	19,966
$ 205,672	$ 188,451	$ 128,145	$ 49,722	$ 221,971	$ 265,129	$ 222,238
192,886	190,103	170,789	192,823	191,460	182,913	171,870
35,561	35,362	20,617	33,683	39,795	39,772	37,826
92,835	125,716	148,525	149,889	147,567	155,102	90,499
299,630	256,594	170,539	117,671	289,235	329,739	317,392
19.78	15.99	7.38	2.09	16.95	21.09	—
$ 729,143	$ 664,246	$ 704,392	$ 760,946	$ 684,419	$ 670,830	$ 602,404
84,200	85,900	84,500	106,000	105,700	103,600	97,500
73,216	79,848	85,028	86,815	87,750	81,844	70,153
1,663,384	1,663,634	1,664,302	1,664,516	2,064,516	2,064,516	—
10,015,259	9,997,992	9,997,290	9,997,064	9,982,079	9,944,488	9,909,822

Consolidated Balance Sheet

December 31, 1967 and 1966

Assets	1967	1966
Current Assets		
Cash and marketable securities, at cost	$ 33,340,160	$ 43,776,584
Accounts receivable—United States and Canadian Governments	36,184,895	38,326,999
Other trade receivables, less reserves	85,143,521	76,751,642
Unreimbursed expenditures and estimated profits on cost reimbursement and long-term contracts in process (Note 1)	246,614,326	181,192,092
Inventories, at the lower of cost or market, less advance and progress payments	186,473,988	137,565,138
Prepaid expenses	8,979,936	5,879,986
Total Current Assets	596,736,826	483,492,441
Other Assets		
Equity in net assets of unconsolidated subsidiaries (Note 5)	14,851,278	13,018,123
Receivables not currently due and other assets	23,915,228	24,459,928
	38,766,506	37,478,051
Property, Plant and Equipment (Note 6)		
Land and buildings, at cost	181,572,854	167,616,215
Machinery and equipment, at cost	473,562,556	429,898,744
	655,135,410	597,514,959
Less—Reserves for depreciation, etc.	370,230,036	359,760,529
	284,905,374	237,754,430
	$ 920,408,706	$ 758,724,922

The accompanying notes are an integral part of the above statement.

Liabilities and Share Owners' Equity	1967	1966
Current Liabilities		
Notes payable	$ 56,617,360	$ 35,491,500
Bank drafts payable	39,489,503	25,188,877
Current installments on long-term debt (Note 2)	10,820,842	6,846,404
Accounts payable and accrued expenses	258,301,302	185,211,018
Accrued salaries and wages	36,458,426	37,667,272
United States and Canadian income taxes	21,486,311	29,844,077
Customers' deposits and advances in excess of costs	8,101,741	5,701,393
Total Current Liabilities	431,275,485	325,950,541
Non-Current Liabilities		
Long-term debt (Note 2)	125,886,208	131,249,495
Other liabilities	8,298,919	—
Deferred income taxes (Note 7)	17,550,941	13,967,343
	151,736,068	145,216,838
Minority Interests in Subsidiary Companies	1,310,965	1,455,831
Share Owners' Equity		
Preferred Stock, par value $1 per share (Note 3)		
Authorized—1,500,000 shares		
Outstanding—None	—	—
Common Stock, par value $1 per share (Note 4)		
Authorized—30,000,000 shares		
Outstanding—10,435,706 shares at end of 1967, after deducting 35,000 shares in Treasury	10,435,706	10,324,596
Capital Surplus	49,155,464	45,925,338
Earned Surplus (Note 2)	276,495,018	229,851,778
	336,086,188	286,101,712
	$ 920,408,706	$ 758,724,922

The accompanying notes are an integral part of the above statement.

Statement of Consolidated Income

For the Years Ended December 31, 1967 and 1966	1967	1966
Net Sales	$2,253,336,241	$1,796,990,612
Cost of Sales	2,163,916,638	1,704,681,076
Profit from operations	89,419,603	92,309,536
Other Income (Expense):		
Interest—net	(10,067,142)	(5,018,541)
Miscellaneous—net	5,136,675	2,379,431
	(4,930,467)	(2,639,110)
Profit Before Income Taxes and Gain on Disposition of Securities	84,489,136	89,670,426
Provision for Income Taxes	33,200,000	35,716,000
Income Before Gain on Disposition of Securities	51,289,136	53,954,426
Gain on Disposition of Securities, less applicable taxes of $1,605,000 and $1,484,000	5,736,576	4,452,147
Net Income	57,025,712	58,406,573
Less—Dividends on Convertible Preference Stock	—	661,100
Available for Common Share Owners	$ 57,025,712	$ 57,745,473
Per Common Share of Stock		
Income before Gain on Disposition of Securities	$ 4.91	$ 5.16
Gain on Disposition of Securities less applicable taxes	.55	.43
Net Income	$ 5.46	$ 5.59

Statement of Consolidated Earned Surplus

For the Years Ended December 31, 1967 and 1966	1967	1966
Earned Surplus at beginning of year	$ 229,851,778	$ 185,771,490
Net income	57,025,712	58,406,573
	286,877,490	244,178,063
Deduct:		
Excess of redemption price over liquidating value of 781,442 shares of convertible preference stock	—	2,952,377
Excess of cost of marketable securities over par value of 35,000 shares of common stock of the Corporation received in exchange therefor	—	423,089
Dividends—Common stock ($1 per share)	10,382,472	10,289,719
Dividends—Convertible preference stock	—	661,100
	10,382,472	14,326,285
Earned Surplus at end of year	$ 276,495,018	$ 229,851,778

The accompanying notes are an integral part of the above statements.

Statement of Consolidated Source and Use of Working Funds

For the Year Ended December 31, 1967

	1967
Source of Working Funds:	
Net Income	$ 57,025,712
Provision for depreciation, amortization and depletion	37,996,388
Sale and retirement of property, plant and equipment	11,803,168
Increase in deferred income taxes and other non-current liabilities	11,882,517
Proceeds from stock options exercised	3,341,236
	122,049,021
Use of Working Funds:	
Expenditures for property, plant and equipment	96,950,500
Payment of dividends	10,382,472
Long-term debt	5,363,287
Other—net	1,433,321
	114,129,580
Increase in Working Funds	7,919,441
Working Funds:	
December 31, 1966	157,541,900
December 31, 1967	$ 165,461,341

Statement of Consolidated Capital Surplus

For the Years Ended December 31, 1967 and 1966

	1967	1966
Capital Surplus at beginning of year	$ 45,925,338	$ 41,142,972
Excess of proceeds over par value of common stock sold to employes under stock options	3,230,126	3,622,680
Excess of paid-in capital of Dynatronics, Inc. acquired in a pooling of interests over par value of 91,607 shares of common stock issued by the Corporation	—	827,242
Excess of liquidating value of convertible preference stock over par value of common stock issued therefor	—	332,444
Capital Surplus at end of year	$ 49,155,464	$ 45,925,338

The accompanying notes are an integral part of the above statements.

Notes to Financial Statements

1. Method of Profit Accrual:

Profits are recorded on all cost reimbursement type contracts and certain long-term contracts prior to completion thereof where, in the opinion of management, such profits can be reasonably estimated after taking into consideration the stage of completion and the estimated final costs and prices.

2. Long Term Debt:

Long-term debt includes notes of $124,000,000 payable to an insurance company with interest from 5% to 5½%. The terms of the agreements relating to such notes provide, among other things, for (a) payments of $8,000,000 in 1968, which amount is included in current installments on long-term debt as of December 31, 1967, $8,000,000 annually in 1969 through 1977, $25,500,000 in 1978, $16,500,000 in 1979 and the balance of $2,000,000 in 1980; (b) consolidated working capital, as defined in the agreements, of not less than $150,000,000; and (c) restrictions on the amount available for cash dividends on the common stock of the Corporation to 70% of consolidated net income as defined in the agreements subsequent to December 31, 1963, less the sum of cash dividends paid or declared subsequent to that date. As of December 31, 1967, consolidated working capital totaled $165,461,341 and earned surplus restricted under (c) aggregated $174,629,073.

There are other long-term notes and mortgages aggregating $9,886,208 after deducting current installments, due in varying amounts to 1981 with interest from 3% to 7%.

3. Preferred Stock:

On April 27, 1967, the Certificate of Incorporation was amended to authorize 1,500,000 shares of Preferred Stock, par value $1 per share, issuable in series, with the rights, preferences and limitations of each series to be determined by the Board of Directors.

4. Common Stock:

The Qualified Stock Option Plan, approved by the share owners in 1964, authorizes the issuance of an aggregate of 475,000 shares of common stock upon exercise of options to be granted under the Plan. The purchase price of shares under option shall not be less than 100% of the fair market value of the common stock at the date the option is granted, and the options may not have a term of more than five years from date of grant. Options become exercisable on such terms and conditions as the Stock Option Committee, appointed by the Board of Directors, shall, in its discretion, prescribe. Options granted become exercisable in cumulative installments of 25% on each of the first four anniversaries of the date of grant.

Under the Corporation's Restricted Stock Option Plan, approved by the share owners in 1951, the price to be paid for the shares covered by each option is 95% of the fair market value thereof on the date the option was granted. Options under this Plan were granted for a seven-year period and are exercisable in installments from two to five years from date of grant. No additional options may be granted under this Plan, and the final option expires in December, 1970.

Information with respect to options for the year 1967 under each of the Plans is summarized below:

	Qualified Plan	Restricted Plan
Number of shares under stock options:		
Outstanding January 1, 1967	305,450	111,490
Add (deduct):		
Granted	59,750	—
Exercised	(42,480)	(68,630)
Cancelled	(15,575)	(5,180)
Outstanding December 31, 1967	307,145	37,680
Aggregate price of shares under stock options:		
Granted during 1967	$3,358,040	$ —
Outstanding December 31, 1967	$14,280,667	$971,393

Of the common stock authorized but unissued, 451,425 shares are reserved for options outstanding or issuable under the Corporation's stock option plans at December 31, 1967.

5. Unconsolidated Finance Subsidiary:

Stromberg-Carlson Credit Corp., an unconsolidated subsidiary, purchases from the Corporation or a consolidated subsidiary (a) notes issued by independent telephone companies in connection with the sale of telephone equipment, and (b) notes and other receivables resulting from aircraft sales and equipment leases. Following is a summary of the balance sheet of the Credit Corp. as of December 31, 1967:

Notes receivable from independent telephone companies	$ 91,521,500
Notes and receivables on aircraft sales and equipment leases	22,136,582
Cash and other assets	2,849,977
	$116,508,059
Notes payable	$ 81,206,000
Short-term borrowings	28,506,147
Other liabilities	3,897,299
Share owner's equity	2,898,613
	$116,508,059

The Corporation or a consolidated subsidiary has guaranteed payment of the notes payable and short-term borrowings, and in the event of default has agreed to repurchase notes and receivables on aircraft sales and equipment leases.

6. Properties:

Property, plant and equipment at December 31, 1967 includes land of $31,438,554. Provisions for depreciation, amortization and depletion aggregated $37,996,388 in 1967 and $32,661,725 in 1966.

The Corporation leases from the United States Govern-

ment substantial portions of plant facilities used in the operation of certain divisions.

7. Income Taxes:
Deferred income taxes are applicable primarily to accelerated depreciation deducted for tax purposes but not for financial reporting. Such deferred taxes will offset amounts payable in subsequent years when depreciation provisions included in financial statements exceed those allowable for income tax purposes.

Investment tax credits applicable to property additions are reflected in the Statement of Consolidated Income as a reduction of the provision for income taxes.

United States income tax returns of the Corporation are subject to review by the Internal Revenue Service for all years subsequent to 1961.

8. Employes' Retirement Plans:
The Corporation and Subsidiaries have a number of retirement plans covering substantially all employes. Unfunded actuarial liability under the plans was approximately $89,000,000 at December 31, 1967. The Corporation's present policy is to amortize unfunded actuarial liability, including interest thereon, over a period of twenty years subsequent to 1965. The cost of all plans for 1967 was $28,007,713, including $6,101,655 for amortization of unfunded actuarial liability. Accrued retirement costs are paid into trust funds which may be used only for benefits provided by the Plans.

9. Liquid Carbonic Corporation:
Under the judgment of a Federal District Court the Corporation must divest itself of Liquid Carbonic Corporation together with its holdings of stocks of foreign companies engaged in the production, distribution and sale of carbon dioxide or other industrial gases. Negotiations with prospective purchasers were in progress at year end.

Net sales of Liquid Carbonic operations for the year 1967 included in consolidated sales of the Corporation amounted to $66,529,000 or 3.0% after excluding $2,272,000 of intercompany sales. Sales of the unconsolidated subsidiaries not included in consolidated sales were $15,937,000. Net income of the Corporation and subsidiaries includes earnings of Liquid Carbonic Corporation and subsidiaries of approximately $4,985,000 before allocation of Corporate Office expense, or 8.7% of consolidated net income, compared with 8.0% in 1966.

10. Classifications:
Certain accounts in the December 31, 1966 consolidated financial statements have been restated to conform to the classifications used at December 31, 1967.

11. Contingent Liabilities:
A substantial portion of sales for 1963 through 1967 is subject to review by the United States Renegotiation Board. Management believes that the Corporation will not be required to make refunds under the Renegotiation Act of 1951, and consequently no provision has been made therefor.

In addition, there were other contingent liabilities with respect to guarantees, law suits and other matters arising in the ordinary course of business. In the opinion of management, reasonable reserves have been provided for contingent liabilities.

12. General Atomic:
The General Atomic Division was sold during the year for an amount which exceeded by approximately $9.0 million (after taxes) the net book value of the Division's assets; however, this non-operating gain was not recorded in 1967 because it is subject to contingencies expected to be determined in 1968.

The operations of the General Atomic Division, which were primarily of a Research and Development nature, resulted in a charge against consolidated profit of approximately $2.4 million after income taxes in 1967.

Auditors' Report

To the Share Owners and the Board of Directors of
General Dynamics Corporation:

We have examined the consolidated balance sheet of General Dynamics Corporation (a Delaware corporation) and subsidiaries as of December 31, 1967, and the related statements of consolidated income, surplus and funds for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We were unable to obtain confirmation of receivables from the United States and Canadian Governments; however, we have applied other auditing procedures as to such receivables. We have previously examined and reported on the financial statements for the preceding year.

In our opinion, the accompanying consolidated balance sheet and statements of consolidated income, surplus and funds present fairly the financial position of General Dynamics Corporation and subsidiaries as of December 31, 1967, and the results of their operations and the source and disposition of funds for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

New York, N. Y.,
January 31, 1968. Arthur Andersen & Co.

General Dynamics Corporation

One Rockefeller Plaza, New York, New York 10020

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Roger Lewis

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Frank W. Davis
John C. Franklin
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Divisions

Convair Division, San Diego, California
Electric Boat Division, Groton, Connecticut
Electro Dynamic Division, Avenel, New Jersey
Electronics Division, Rochester, New York
Fort Worth Division, Fort Worth, Texas
Material Service Division, Chicago, Illinois
Pomona Division, Pomona, California
Quincy Division, Quincy, Massachusetts

Subsidiaries

Canadair Limited, Montreal, Quebec, Canada
Freeman Coal Mining Corporation, Chicago, Illinois
Liquid Carbonic Corporation, Chicago, Illinois
Marblehead Lime Company, Chicago, Illinois
Stromberg-Carlson Corporation, Rochester, New York
The United Electric Coal Companies, Chicago, Illinois

Transfer Agents

Bankers Trust Company, New York, New York
Bank of America National Trust and Savings Association, San Francisco, California
The First National Bank of Jersey City, Jersey City, New Jersey
The First National Bank of Chicago, Chicago, Illinois
Montreal Trust Company, Montreal, Quebec, and Toronto, Ontario, Canada

Registrars

The Chase Manhattan Bank, New York, New York
Wells Fargo Bank, San Francisco, California
American National Bank and Trust Company of Chicago, Chicago, Illinois
The Royal Trust Company, Montreal, Quebec, and Toronto, Ontario, Canada

Stock Exchange Listings

New York Stock Exchange
Midwest Stock Exchange
Pacific Coast Stock Exchange
Montreal Stock Exchange
Toronto Stock Exchange

Auditors

Arthur Andersen & Co., New York, New York

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